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IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

No. 80-1353

VAN DYK RESEARCH CORPORATION,

Petitioner,

v.

XEROX CORPORATION,

Respondent.

REPLY IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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STATEMENT IN ACCORDANCE WITH SUPREME COURT RULE 28.1

Petitioner's Rule 28.1 statement is found in its Petition, filed on February 11, 1981, at page i, n.1.

DISCUSSION

In Respondent's Brief In Opposition ("Respondent's Brief"), Xerox selects evidence which it claims supports the District Court's determination that Van Dyk was not injured by Xerox' patent practices. In so doing, Xerox does not fairly describe the record concerning, for example, the testimony of Peter Bennett of Merrill Lynch that "virtually" all investors who were interested in investing in Van Dyk were seriously concerned about the threat of patent litigation by Xerox. (A. 512). In Respondent's Brief, selective use is made of some of Bennett's notes in a disingenuous effort to demonstrate that virtually all potential investors were not concerned about Xerox' patents.[1]

Similarly, Xerox' treatment of Agfa Gevaert's expressed concern about Xerox' patents both in the United States and in Europe is simply erroneous.[2] The fact is that Van Dyk could not give patent assurances to Agfa, and therefore had little choice but to deal with a financially distressed Apeco Corporation, a company which did not demand patent clearance. The threat of Xerox patent litigation was not illusory; on April 2, 1973, within days after the public announcement of Apeco's plan to loan Van Dyk $5,000,000, Van Dyk received the following letter from Xerox' Patent Department, which was timed to sabotage the Apeco financing:

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[1] Xerox' cross-examination of Bennett, a disinterested witness, elicited the following testimony:

> Well, you know there are several important factors which were stumbling blocks to various institutions and *patents certainly were one of those major stumbling blocks.* I could not rank it whether it was patents, markets, Xerox competition or what. I couldn't rank those but it certainly was one of the *important* problems. (A. 571) (emphasis added).

Nor does Xerox refer to Bennett's notes concerning, for example, the attitude of G.E. Pension Fund, a potential investor in Van Dyk: "Nobody can break Xerox monopoly except IBM." (PX 19).

[2] See e.g. Van Dyk's Petition, p. 11, n.12, concerning Xerox' European patent accumulations.

> In view of the recent introduction of the Van Dyk 4000 plain paper copier, Xerox Corporation requests access to this machine apropos inspecting it or otherwise analyzing it for patent infringement purposes. * * * I would very much appreciate your early attention to this matter. (PX 34).

Eight of the nine patents which the Van Dyk 4000 was alleged by Xerox' Patent Department to have infringed have been found invalid. (See *infra*, and see Van Dyk's Petition, pp. 5-6). It was the Xerox Patent Department which secured those patents, after failing to disclose the prior expired or expiring Xerox patents to the United States Patent Office.

It is evident from the record, as described in Van Dyk's Petition, that numerous firms interested in marketing the Van Dyk 4000, and large investors which were considering providing substantial funds to Van Dyk had significant and well-founded concern about the threat of patent litigation by Xerox, and considered that threat a material deterrent to trading with or investing in Van Dyk. It is simply not possible to conclude otherwise.

Unlike Xerox, the Court of Appeals, in the concurring opinion (in a conclusion not disputed in the majority opinion), recognized that Van Dyk's evidence of the fact of damage "was sufficient to permit the trier of fact to make the causal connection suggested by Van Dyk and would have supported a jury verdict for damages, assuming that Van Dyk surmounted the hurdles of proving liability and producing sufficient evidence from which a reasonable damage calculation could be made," and recognized further that "plaintiff's case was not deficient in the quantum of evidence needed to present the issue of fact to the jury." (App. A, p. 13a).

The relief which Van Dyk sought in the Court of Appeals was a remand of the case to the District Court for consideration of the decisions of the United States Patent Office, issued subsequent to the District Court's judgment,

which contradicted the District Court's Findings of Fact on the crucial patent abuse issue, and which demonstrated that, had the District Court properly considered Van Dyk's evidence on this issue, it would have found (as did the United States Patent Office) that Xerox was not simply an innocent innovator.[3]

[3] In Respondent's Brief, p. 12, n.8, Xerox quotes the oral argument on appeal out of context, contending that Van Dyk counsel conceded that the proceedings in the Patent Office are not relevant to any "bad faith" by Xerox in procuring crucial patents without disclosing prior art. Van Dyk counsel made no such concession; indeed, counsel could hardly have done so, since the Patent Commissioner's Office, *sua sponte,* determined to investigate the issue of fraud. (See Van Dyk Petition, p. 9, n.11). Van Dyk counsel stated that the Patent Office investigation did not relate to patent *misuse* (a term normally applied to unlawful use of a lawfully acquired patent, e.g. as part of a tying arrangement). Counsel did not state that the investigation was unrelated to patent *abuse*; it is so related, and such abuse is the very charge Van Dyk made before the District Court. (See, e.g. Oral Argument Tr. pp. 10, 55-56). Counsel discussed Van Dyk's charges of accumulation of patents which were "not legitimate patents", concluding:

> If that isn't patent misuse, it's not technically where you have a tie-in or something like that, but it is certainly recognized in antitrust doctrine as very serious conduct (Oral Argument Tr. p. 10).

The cases cited by Xerox on page 12, n.7 of Respondent's Brief, for the proposition that the Court of Appeals could not consider the relevance of the United States Patent Office decisions, since they were issued after the filing of the District Court's opinion, are inapposite. Those cases (none relating to patents) merely state the general rule that an appellate court will not consider matters outside of the record which are first raised on appeal. On the other hand, there is also no dispute that (as here), the "normal rule is subject to the right of an appellate court in a proper case to take judicial notice of new developments not considered by the lower court [citations omitted]," including administrative action by United States government agencies. Moreover, for purposes of "judicial economy", the appellate court will remand the case for reconsideration by the District Court in light of the new developments. *Landy v. Federal Deposit Insurance Corporation,* 486 F.2d 139, 150-51 (3d Cir. 1973), *cert. denied* 416 U.S. 960 (1974). That is what Van Dyk requests here — not, as Xerox implies, a review by this Court or by the Court of Appeals of all of the District Court's Findings of Fact. See also, *Zahn v. Transamerica Corporation,* 162 F.2d 36, 48 n.2 (3d Cir. 1947).

If the Court of Appeals believed, as it did, that Van Dyk's evidence on the fact of damage issue would have supported a verdict for Van Dyk, assuming proof of a violation and of the amount of damage, the case should have been remanded to the District Court for reconsideration of the patent issue as well as the other important issues. This is especially true where the District Court's decision rests upon its perception that Xerox' market position was acquired and maintained solely as a result of Xerox' "research," its "risk taking," its "innovation," its "inventiveness," and a resultant lawful patent monopoly.

In summarizing its lengthy Findings of Fact, the District Court paid tribute to Xerox' creativity:

> Xerox has not acquired or maintained its market position by any exclusionary conduct. Instead, its position is based upon its research, its risk taking and innovation, its inventiveness, and its vast expenditures to constantly improve its technology. While it has been and is an aggressive competitor, it has been a lawful competitor. (App. B., p. 117a).
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> * * * * * *
>
> Xerox' patent policy and program were not adopted or pursued with anticompetitive intent or purpose. Its accumulation of patents was protected conduct, the result of research efforts to develop and improve its products. It could and did no more than lawfully protect itself against competitor copying of its products and insure that it would not be blocked from the use of inventions which might prove useful in the future. [Citation to cases and to U.S. Constitution, Article I § 8, cl. 8 omitted].
>
> Thus, Xerox is not guilty of "wrongly using the patent system to restrain trade", as charged by Van Dyk.* * * * It did not accumulate patents simply in order to maintain dominance, as Van Dyk charges. . . . (App. B., p. 120a).[4]

[4] The critical Xerox patents were described by Xerox witnesses to the District Court, with great emphasis being placed on their exceptional importance to xerography and to Van Dyk's appropriation of this innovative patented technology in the Van

It is simply not possible to reconcile these encomiums with the rejections by the United States Patent Office of the very patents which, according to Xerox, allegedly went to the "heart of xerography", and the significance of which was so important to Xerox' success against Van Dyk in the District Court.[5]

The issue which the Court of Appeals refused to address relates not only to Xerox' patent abuse, but to the central, related question of how the Court of Appeals could rely upon Findings by the District Court which, after praising Xerox for its patent acumen, thereafter concluded that Van Dyk was not injured by Xerox' lawful patents.

Dyk 4000. The District Court accepted the entire scenario and totally disregarded all of Van Dyk's evidence to the contrary. The District Court even concluded that Xerox' conduct was "reflective of the *best* of our free marketplace." (App. B., p. 120a) (emphasis added).

[5] The magnitude of the District Court's error and the validity of Van Dyk's evidence are further highlighted by decisions of the United States Patent Office issued since the filing of Van Dyk's Petition for a Writ of Certiorari on February 11, 1981. As of the date of this Reply, Xerox' appeal of the Patent Examiner's rejection of *all* claims in its Van Dorn patent was unanimously affirmed by the Patent and Trademark Office Board of Appeals. Moreover, Official Actions have now been issued by the Patent Examiners in two of the four pending Xerox Continuation Reissue Applications. In both Official Actions, *all* of the Xerox patent claims have again been rejected. (Xerox elected not to mention these decisions in Respondent's Brief.) Xerox repeatedly refers to the decisions in the Patent Office as "preliminary" though there are both Initial and Final Actions rejecting the patents, though Official Actions have issued rejecting all claims in two Continuation Applications, and though the Board of Appeals has unanimously affirmed the rejection of the Van Dorn patent. Moreover, eight of the nine patents — not seven as Xerox claims — have been found invalid. Since Van Dyk had filed a late response with respect to one Action which would have resulted in a default victory to Xerox, the Commissioner's Office, in view of the importance of the proceeding, directed the Patent Examiner to issue an Advisory Opinion for submission to the District Court in the patent action. The Advisory Opinion rejects the Xerox patent. Xerox elected not to contest the issue further in the Patent Office, although it was entitled to do so.

It is true, and Van Dyk has never denied, that there were other events in Van Dyk's corporate existence which caused it injury, including Apeco's concealment of its distressed financial condition, Mayflower's problems with the SEC, and the termination of the SCM agreement. It is equally true and equally apparent, however, that "a material cause" of injury to Van Dyk from the first day it sought to secure capital and attempted to enter into business relationships with firms such as Agfa, Konishiroku, 3M and others, were those Xerox patents which had been unlawfully obtained, and which Xerox intended to employ against Van Dyk and any firm dealing with Van Dyk, in order to cripple what Xerox perceived to be "the first visible competitive thrust into the heartland of Xerox profits" by a small firm with "a very strong product." (A. 492, 1000; PX 69 at 443541, 443543). In sum, the Findings accepting Xerox' testimony exonerating its patent practices cannot be separated logically from the Findings which accepted Xerox' position that its patent policies had no material effect upon Van Dyk's ability to compete. A remand was therefore required.[6]

Respondent's Brief contains numerous misstatements, to the most significant of which Van Dyk responds in this

[6] Respondent's Brief repeatedly refers to the Van Dyk 4000 as "obsolete", an adjective which does not appear in any Xerox document. The Van Dyk copier was not considered obsolete by Xerox when it replaced Xerox equipment throughout installations of the Federal Government and constituted Xerox' "most severe problem" in the Middle Atlantic States. (PX 67). The Xerox executive who was responsible for Federal Government marketing testified that "the [Van Dyk] machine had attracted a great deal of interest and a sizable number of government personnel were visiting the site." (A. 491). He further testified that the Van Dyk copier "caused concern that a machine of some obvious technological attractiveness was entering that market", and that his superiors stated that "patent litigation should be considered a competitive — I don't want to say 'weapon' — a competitive tactic as well as those tactics one would engage in in the marketplace." (A. 492-493).

From Van Dyk's market entry in 1972 until it filed under Chapter XI, Xerox continued to report that Van Dyk 4000 was a serious threat, "throughout all our major accounts." (See e.g. PX 86; Van Dyk's Petition, pp. 3-4).

Reply. A prime example is Xerox' statement (p. 6) that in October, 1975, "[u]nable to pay its suppliers, Van Dyk filed a petition for an arrangement under Chapter XI of the Bankruptcy Act and lawsuits against Apeco, SCM, and Xerox." As Xerox well knows, Apeco sued Van Dyk first (in 1974), a suit to which Van Dyk responded by filing its own claim, and SCM sued Van Dyk, asserting a claim concerning parts and supplies, shortly after Van Dyk entered Chapter XI. (Van Dyk filed a counterclaim to that suit). The only suit instituted first by Van Dyk was that against Xerox, seven months prior to Van Dyk's Chapter XI filing.

Xerox makes several claims concerning two other issues in this case, to which Van Dyk responds briefly below. While acceptance of Van Dyk's Petition would not require this Court to resolve these issues, Van Dyk submits this response in order to demonstrate the lack of support for Xerox' claims.

With respect to Xerox' "rental only" policy, Xerox claims that "contrary to Van Dyk's charge that Xerox rented its machines on a short term basis for anticompetitive purposes, Xerox' rental policies were a response to the demand of its customers" (Respondent's Brief, p. 7, n.5), and that "[t]he figures quoted by Van Dyk in its petition concerning the 'assigned cost' of various Xerox machines omit . . . huge research and development costs. Not surprisingly, the sales prices set by Xerox to recover part of those R & D costs are much higher." (Respondent's Brief, p. 4, n.2). It should be clear that, when Xerox established a $14,000 purchase price for the Xerox 2400 to the GSA, Xerox undoubtedly included sufficient margin to recover research and development costs, and more. Thus, when it raised the price to the GSA from $14,000 to $27,900, Xerox did so for one reason: to prevent the purchase of the equipment, and not to recover "R & D" costs. (See Van Dyk's Petition, pp. 13-14).

Other Xerox internal documents belie Xerox' claim concerning the genesis of its rental only policy. (See, e.g. Van Dyk's Petition, pp. 11-14). In addition, Xerox' Assistant Treasurer described its rental only policy as "[n]ext to the decision to take on xerography, *the most important decision made by our management*" and explained that it was this rental only policy which imposed "staggering capital requirements and a balance sheet which began to look like that of a public utility rather than a manufacturing company." (PX 430 at 4) (emphasis added). Finally, the profits that were derived from Xerox customers who were required to pay every time they made a copy on their rented Xerox copiers prompted Xerox' Vice-President to preface his financial report to President McColough with the comment "start drooling." (PX 433 at 432174).[7]

With respect to the relevant market issue, Xerox argues that "the relevant copier/duplicator market includes coated paper and offset machines as well as the plain paper copiers manufactured by Xerox and Van Dyk . . ." and that "Xerox had no ability to exclude competition from, or control prices in that market". (Respondent's Brief, p. 7, n.5). In another case, however, *SCM Corporation v. Xerox Corporation*, Docket No. 79-7017, the Court of Appeals for the Second Circuit, in a decision issued on March 12, 1981, observed that "Xerox concedes that its plain paper copiers eventually formed an independent relevant product market," (Slip Op. p. 14) and that "Xerox does not dispute that it achieved monopoly power in the relevant market and

[7] Dr. Edwin Mills of Princeton University, Van Dyk's expert in economics, reported that Xerox' return on capital, many times that of a normal firm (A. 184), was indicative of "extraordinarily strong market power." (A. 185-86). Dr. Mills' testimony corroborated the observation by Xerox' Pricing Manager, who candidly admitted that "as the dominant factor in the industry Xerox has *a very large vested interest in maintaining high price levels.*" (PX 450 at 012892-93) (emphasis added). This same conclusion was reached by Xerox in 1972 (PX 1126 at 0121870) as Van Dyk prepared to enter the marketplace by offering Van Dyk equipment to all customers at from 16% to nearly 50% below Xerox' lowest rental price (a price which was available only to Xerox' largest accounts). (PX 79, 80, 86, 88, 106, 110 at 2).

submarket by 1969. . . ." (Slip Op. p. 13). Thus, while Xerox conceded in the Second Circuit that its plain paper copiers constituted a relevant submarket, it argued in the Third Circuit that plain paper copiers competed intensively with coated paper copiers and offset devices, and that all of these products constituted the only relevant market.[8]

It is not surprising that the Court of Appeals, in *Van Dyk v. Xerox*, which elected not to affirm the District Court's Findings concerning patent practices and "rental only", also did not affirm the District Court's findings on relevant market. The Court of Appeals' puzzlement with Xerox' position is reflected in the Court's statements:

> Mr. McAlee, if it doesn't interrupt you too much, I wonder if you could answer [if] Judge Lacey didn't use the wrong standard in defining the market when he talked about a continuum in the market which went from coated paper copiers at the lower end to offset at the higher end, which makes it sound a little bit as if automobiles might be in the same market with bicycles on one end and the Learjet at the other.
>
> * * * * * *

[8] In *SCM v. Xerox*, SCM did not contest at trial the validity of Xerox' patents, and the issue was never presented in that case. See, *SCM v. Xerox*, 463 F. Supp. 983, 985 n.3 (D. Conn. 1978). The issue presented to the Second Circuit was whether a monopolist's unilateral refusal to license patents could ever give rise to a damage award. Without ruling on that issue, the Court of Appeals determined that Xerox' acquisition of the patents at issue in *SCM* (in the 1950s) could not have been unlawful, since, at the time, no relevant market or submarket for plain paper copiers existed. (The first plain paper copier was not marketed until 1960). (Slip Op. at 8, 12-13, 18-20, 22-23). Therefore, the Court ruled that Xerox' subsequent refusal to license could not have been illegal. (Slip Op. at 22-23, 26-27, 29-30). By contrast, (as Xerox counsel repeatedly urged before the District Court) Van Dyk's claims are different. Van Dyk's claims are not based upon a unilateral refusal to license patents, nor upon the existence or non-existence of a relevant market in the 1950s. The patents which are central to Van Dyk's claims (in particular the issues presented in Van Dyk's Petition) were alleged "improvement" patents, which Xerox acquired in order to extend its monopoly. *Van Dyk v. Xerox* is the first case in which questions relating to the deliberate recreation of patents has been litigated.

> Why isn't it like commercial banking, as an example, in which the Supreme Court said, Oh, sure, we recognize that there is lots of competition at different levels to commercial banking, savings and loans, et cetera, but nevertheless we find that commercial banking is a realistic submarket, which is the same thing as a market. A submarket is no different. How does this differ from that? (Oral Argument Tr., pp. 26-27, 42).

The Court of Appeals affirmed the District Court by ruling upon only one issue: the "fact of damage."

Van Dyk respectfully submits that the Court of Appeals did make a "very obvious and exceptional" error when it refused to remand this case to the District Court for reconsideration of its Findings of Fact, in light of the decisions of the United States Patent Office which corroborate Van Dyk's evidence demonstrating patent abuse, and which require the District Court to reappraise its other Findings, particularly on the related issue of the "fact of damage."

CONCLUSION

For the reasons stated above, and in its Petition, Van Dyk's Petition for a Writ of Certiorari should be granted.

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Respectfully submitted,

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